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FINANCIAL SERVICES

Prepare for Life

Winter 2022

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A NEW YEAR rings in SUPER CHANGES

New rules coming into force on July 1 will create opportunities for older Australians to boost their retirement savings and younger Australians to build a home deposit, all within the tax-efficient superannuation system.

Using the existing First Home Super Saver Scheme, people can now release up to $50,000 from their super account for a first home deposit, up from $30,000 previously.[i]

Another change that will help low-income earners and people who work in the gig economy is the scrapping of the Super Guarantee (SG) threshold. Previously, employees only began receiving compulsory SG payments from their employer once they earned $450 a month.[ii]

But the biggest potential benefits from the recent changes will flow to Australians aged 55 and older. Here's a rundown of the key changes and potential strategies.

Work test changes[iii]

From July 1, anyone under the age of 75 can make and receive personal or salary sacrifice super contributions without having to satisfy a work test. Annual contribution limits still apply and personal contributions for which you claim a tax deduction are still not allowed.

Previously, people aged 67 to 74 were required to work for at least 40 hours in a consecutive 30-day period in a financial year or be eligible for the work test exemption.

This means you can potentially top up your super account until you turn 75 (or no later than 28 days after the end of the month you turn 75). It also opens potential new strategies for a making big last-minute contribution using the bring-forward rule.

Extension of the bring-forward rule[iv]

The bring-forward rule allows eligible people to "bring forward" up to two years' worth of non-concessional (after tax) super contributions. The current annual non-concessional contributions cap is $110,000, which means you can potentially contribute up to $330,000.

When combined with the removal of the work test for people aged 67-75, this opens a 10-year window of opportunity for older Australians to boost their super even as they draw down retirement income.

Some potential strategies you might consider are:

- Transferring wealth you hold outside super into super to take advantage of the tax-free environment of super in retirement phase
- Withdrawing a lump sum from your super and recontributing it to your spouse's super, to make the most of your combined super under the existing limits
- Using the bring-forward rule in conjunction with downsizer contributions when you sell your family home.

Downsizer contributions age lowered to 60[v]

From July 1, you can make a downsizer contribution into super from age 60, down from 65 previously. The downsizer rules allow eligible individuals to contribute up to $300,000 from the sale of their home into super. Couples can contribute up to this amount each, up to a combined $600,000. You must have owned the home for at least 10 years.

Downsizer contributions don't count towards your concessional or non-concessional caps. And as there is no work test or age limit, downsizer contributions provide a lot of flexibility for older Australians to manage their financial resources in retirement.

Rules relaxed, not removed

The latest rule changes will make it easier for many Australians to build and manage their retirement savings within the concessional tax environment of super. But those generous tax concessions still have their limits.

Currently, there's a $1.7 million limit on the amount you can transfer into the pension phase of super, called your transfer balance cap.[vi] Just to confuse matters, there's also a cap on the total amount you can have in super (your total super balance) to be eligible for a range of non-concessional contributions.[vii]

As you can see, it's complicated. So if you would like to discuss how the new super rules might benefit you, please get in touch.

Combining downsizer and bring-forward contributions

Australians aged between 60 and 74 now have greater flexibility to downsize from a large family home and put more of the sale proceeds into super, using a combination of the new downsizer and bring-forward contribution rules.

Take the example of Tony (62) and Lena (60). Tony has a super balance of $450,000 while Lena has a balance of $200,000. They plan to retire within the next 12 months, sell their large family home and buy a townhouse closer to their grandchildren. After doing this, they estimate they will have net sale proceeds of $1 million.

Under the new rules from 1 July 2022:

- They can contribute $600,000 of the sale proceeds into their super accounts as downsizer contributions ($300,000 each)
- The remaining $400,000 can also be contributed into super using the bring-forward rule, with each of them contributing $200,000.

By using a combination of the downsizer and bring-forward rules, Tony and Lena can contribute the full $1 million into super. Not only will this give their retirement savings a real boost, but they will be able to withdraw the income from their super pension accounts tax-free once they retire.

i https://www.ato.gov.au/individuals/super/withdrawing-and-using-your-super/first-home-super-saver-scheme/
ii https://www.ato.gov.au/General/New-legislation/In-detail/Super/Removing-the-$450-per-month-threshold-for-superannuation-guarantee-eligibility/
iii https://www.ato.gov.au/Individuals/Super/Withdrawing-and-using-your-super/Repealing-the-work-test-for-voluntary-super-contributions/
iv https://www.ato.gov.au/individuals/super/in-detail/growing-your-super/super-contributions---too-much-can-mean-extra-tax/?page=7#Bringforwardarrangements
v https://www.ato.gov.au/Individuals/Super/Growing-your-super/Adding-to-your-super/Downsizing-contributions-into-superannuation/
vi https://www.ato.gov.au/Individuals/Super/Withdrawing-and-using-your-super/Transfer-balance-cap/
vii https://www.ato.gov.au/individuals/super/in-detail/growing-your-super/super-contributions---too-much-can-mean-extra-tax/?page=11

HOW TO MANAGE RISING

RISING INTEREST RATES ARE ALMOST ALWAYS PORTRAYED AS BAD NEWS, BY THE MEDIA AND BY POLITICIANS OF ALL PERSUASIONS. BUT A RISE IN RATES CUTS BOTH WAYS.

Higher interest rates are a worry for people with home loans and borrowers generally. But they are good news for older Australians who depend on income from bank deposits and young people trying to save for a deposit on their first home.

Rising interest rates are also a sign of a growing economy, which creates jobs and provides the income people need to pay the mortgage and other bills. By lifting interest rates, the Reserve Bank hopes to keep a lid on inflation and rising prices. Yes, it's complicated.

How high will rates go?

In early May, the Reserve Bank lifted the official cash rate from its historic low of 0.1 per cent to a still low 0.85 per cent. The reason the cash rate is watched so closely is that it flows through to mortgages and other lending rates in the economy.

To tackle the rising cost of living, the Reserve Bank expects to lift the cash rate further, to around 2.5 per cent.[i] Inflation is currently running at 5.1 per cent and while unemployment is below 4 per cent, annual wages growth of 2.4 per cent is not keeping pace with rising prices.[ii]

So what does this mean for household budgets?

Mortgage rates on the rise

The people most affected by rising rates are likely those who recently bought their first home. In a double whammy, after several years of booming house prices the size of the average mortgage has also increased.

According to CoreLogic, even though price growth is slowing, the median home value rose 16.7 per cent nationally in the year to April to $748,635. Prices are higher in Sydney, Canberra and Melbourne.

The table following shows the impact a rate rise of 1-2 per cent rise would have on monthly mortgage repayments in Australia's capital cities.

INTEREST RATES

How much could mortgage repayments rise for a new owner occupier?

			Monthly mortgage repayments		
	Median value	Loan amount (80% LVR)	Current*	Increase with 1% rise	Increase with 2% rise
Sydney	$1,127,723	$902,178	$3,560	$486	$1,006
Melbourne	$806,144	$644,915	$2,545	$348	$719
Brisbane	$770,808	$616,646	$2,433	$332	$687
Adelaide	$619,819	$495,855	$1,957	$267	$553
Perth	$552,128	$441,702	$1,743	$238	$492
Hobart	$735,425	$588,340	$2,322	$317	$656
Darwin	$501,182	$400,945	$1,582	$216	$447
Canberra	$947,309	$757,847	$2,990	$408	$845

Source: CoreLogic. *Assumes current average variable rate of 2.49%, monthly P&I repayments over 30 years.

The big four banks have already passed on the Reserve Bank's 0.25 per cent increase in the cash rate in full to their standard variable mortgage rates which range from 4.6 to 4.8 per cent. The lowest standard variable rates from smaller lenders are below 2 per cent.[iii]

Still, it's believed most homeowners should be able to absorb a 2 per cent rise in their repayments.

The financial regulator, APRA now insists all lenders apply three percentage points on top of their headline borrowing rate, as a stress test on the amount you can borrow.[iv]

But with prices increasing for food, fuel, childcare and other basics, budgets are tight, and households may need to cut back non-essential spending or increase their hours of work.

Rate rise action plan

Whatever your circumstances, the shift from a low interest rate, low inflation economic environment to rising rates and inflation is a signal that it's time to revisit some of your financial assumptions.

The first thing you need to do is update your budget to factor in higher loan repayments and the rising cost of essential items such as food, fuel, power, childcare, health and insurances. You could then look for easy cuts from your non-essential spending on things like regular takeaways, eating out and streaming services.

If you have a home loan, then potentially the biggest saving involves absolutely no sacrifice to your lifestyle. Simply pick up the phone and ask your lender to give you a better deal. Banks all offer lower rates to new customers than they do to existing customers, but you can often negotiate a lower rate simply by asking.

If your bank won't budge, then consider switching lenders. Just the mention of switching can often land you a better rate with your existing lender.

The challenge for savers

Older Australians and young savers face a tougher task. Bank savings rates are generally non-negotiable, but it does pay to shop around.

Banks have been slower to pass on the full increase in the cash rate to savings accounts. By mid-May only three of the big four had increased rates for savings accounts. Several lenders also announced increased rates for term deposits of up to 0.6 per cent.[v]

High interest rates traditionally put a dampener on returns from shares and property, so commentators are warning investors to prepare for lower returns from these investments and superannuation.

That makes it more important than ever to ensure you are getting the best return on your savings and not paying more than necessary on your loans. If you would like to discuss a budgeting and savings plan, give us a call.

i https://www.rba.gov.au/speeches/2022/sp-gov-2022-05-03-q-and-a-transcript.html

ii https://www.abs.gov.au/

iii https://www.canstar.com.au/home-loans/banks-respond-cash-rate-increase/

iv https://www.apra.gov.au/news-and-publications/apra-increases-banks%E2%80%99-loan-serviceability-expectations-to-counter-rising

v https://www.ratecity.com.au/term-deposits/news/banks-increased-term-deposit-interest-rates

Preparing for the next chapter

Retirement means starting a new chapter of your life, one that gives you the freedom to create your own story, as you decide exactly how you want to spend your time. While retirement may not be part of your immediate plans, there are advantages to giving some thought as to what retirement looks like for you and how to best position yourself, well before you leave the workforce behind.

A time of profound change

Even setting aside the huge financial implications of leaving a regular salary behind, retiring from work represents one of the biggest life changes you can experience.

For most people, the freedom of being able to do whatever you want to do, whenever you want to do it, is pretty enticing. However, it is quite common to have mixed feelings about retiring, particularly as you get closer to retirement. What we do for a living often defines us to some extent and leaving your job can mean a struggle with how you perceive yourself as well as how others view you.

Forge your own path

Don't be tied to preconceptions of what retirement is all about. Retirement has evolved from making a grand departure from the workplace to a more flexible transition that may unfold over several years.

The same applies for your timeframe for retirement. The idea that you 'have' to retire at a certain age is no longer relevant given advances in healthcare and longer lifespans. If work makes you happy and fulfilled, then it can make sense to delay your departure from the workforce.

Planning how to spend your time

It sounds obvious but you'll have more time on your hands so it's important to think about what you want to devote that time to. A study found that 97 percent of retirees with a strong sense of purpose were generally happy and satisfied in retirement, compared with 76 percent without that sense. Think about what gives your life meaning and purpose and weave those elements into your plans.

If you are part of a couple, it's critical to ensure that you are both on the same page about what retirement means to you.

Practical considerations

There's a myriad of practical considerations once you have started to plan how you'll spend your time. Here are a few things you may wish to consider:

- Where do you want to live? Do you want to be close to a city or are you interested in living in a more coastal or rural area? Is there infrastructure and health services you may need as you age?
- What hobbies and activities do you want to be involved in. Do you need to start developing networks for those activities in advance?
- Who do you want to spend time with? If you have children and grandchildren, think about what role you'd like to play in their lives upon retirement.

The best laid plans...

Of course, with all this planning it's also important to acknowledge that the best laid plans can go astray due to factors beyond your control. It's important to keep an open mind and be adaptable.

We are here to help you with the financial side of things to ensure that retirement is not only something to look forward to, but a wonderful chapter of your life once you start to live out your retirement dreams.

i https://www.inc.com/magazine/201804/kathy-kristof/happy-retirement-satisfaction-enjoy-life.html

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